<u>THE MYTH OF THE OPEN JAPANESE MARKET</u>

WHY WE SELL <u>ONE</u> CAR IN JAPAN FOR EVERY <u>120</u> CARS THEY SELL HERE

In the 1950s the Japanese government decided that the creation of a world-class automotive industry was a national priority. Since that time, the government has put policies and practices in place to provide Japanese auto companies a sanctuary market at home and massive competitive advantages abroad. Japan has thwarted every attempt at leveling the playing field. Formal commitments to open the Japanese market have been undermined by replacing overt trade barriers, such as import bans and tariffs, with non-tariff barriers (like currency devaluation policies and distribution limitations). And efforts to negotiate away the non-tariff barriers have been ineffective. **<u>The net result is that imported automobiles account for little more of the Japanese market today (approximately 6%) than they did in the 1960s (1%) when "almost absolute restrictions" were in place. Japan's closed market not only means vastly diminished U.S. exports, but also greatly expanded imports as Japanese auto companies use their unmatched domestic market advantages to build a formidable export platform and other countries' auto production is diverted to the United States.</u>**

1930s — Ford, GM, and Chrysler establish plants in Yokohama. By 1934, American automobiles (imported and domestically produced) account for **<u>90 percent</u>** of the Japanese market.

1936 — To place the automobile industry "in the hands of Japanese both in name and reality, now and in the future," the Diet passes the Automobile Manufacturing Law. The law **<u>prohibits</u>** Ford and GM from producing above current levels, imposes a **<u>50% tariff</u>** on imports of engines and parts, and **<u>bans joint ventures</u>**. With government support, Toyota and Nissan emerge as significant truck producers.

1941 — Japan **<u>expropriates</u>** U.S. auto plants and sales facilities. Places a **<u>ban</u>** on imports.

1951 — Toyota, Nissan, and Ota Jidosha (three main Japanese auto companies) **<u>propose that the Japanese government develop a passenger car industry focusing on small-sized cars</u>**. They ask for equipment investment loans, promotion of equipment and automotive parts imports, a tax differential favoring small cars, and a higher commodity tax on foreign cars.

1952 — Law banning imports expires. Within one year, imports account for **<u>60% of the market</u>**. Chrysler and a number of European firms scope investments in Japan. Smaller Japanese companies explore joint venture opportunities.

- Japan's government – responding to domestic auto company pressure – puts policies in place to close the market to foreign autos, including: (1) preferential allocation of **<u>foreign currency</u>**; (2) providing **<u>technical assistance for auto parts makers</u>**; (3) restricting **<u>foreign investment</u>**; (4) restricting **<u>vehicle imports</u>**; (5) applying **<u>punitive tariffs</u>** on imports; (5) imposing **<u>high commodity taxes</u>** on large cars; (6) establishing complex **<u>regulatory approval procedures</u>**, and; (6) **<u>banning</u>** the use of imported vehicles by government offices. Incentives to purchase smaller cars feed into Japanese consumer preferences in the decades to come.

- Japan also provides the domestic industry preferential government **<u>loans</u>** and other **<u>subsidies</u>**, special **<u>depreciation allowances</u>**, **<u>exemptions</u>** on import duties for certain machinery and equipment, and **<u>authorization</u>** of essential technology imports.

1960s — Imports plummet to **<u>1% of the market</u>**, down from 60% eight years earlier. The Japanese auto industry grows during this period, completing **<u>construction of new mass production facilities</u>** (<u>e.g.</u>, the Toyota Motomachi, Nissan Oppama, Isuzu Fujisawa, Hino Hamura, and Prince Murayama plants). Honda and Mazda, and many smaller companies, also enter the market.

In 1964, the Japanese government issues guidelines **prohibiting Japanese dealers from handling more than one line of vehicle**. Although these requirements are later removed, exclusive dealing becomes a fundamental part of Japanese business practice.

The U.S. General Accounting Office (GAO) reports that "the **'almost absolute' restrictions** which were in force prior to the early 1970s enabled Japanese car producers to develop '. . . world-scale capability with costs low enough to compete in the United States and Europe with prices substantially below [U.S. and European] domestic models.'" (1979). **Japanese exports expand from virtually nothing in 1960 to over half of Japanese production by the mid-1970s. Japan becomes the world's second largest exporter of autos, after the United States**.

1970s Japan comes under pressure under the General Agreement on Tariffs and Trade (GATT), the International Monetary Fund (IMF) and Organization for Economic Cooperation and Development (OECD) to liberalize its import and investment policies. As a result, Japan lowers its most overt barriers such as foreign exchange controls, prohibitions on foreign investment, and prohibitive quotas and tariffs. However, Japan maintains a slate of non-tariff barriers.

- In a 1979 report, GAO finds that cars sell for 50%-82% more in Japan than they do in the United States – e.g., a U.S. subcompact car selling for $4,810 is $7,105 in Japan; a U.S. small sports car selling for $4,915 is $8,605 in Japan; and a U.S. compact car selling for $6,635 is $12,065 in Japan. Non-tariff barriers – high distribution costs stemming from exclusive dealership requirements and barriers to establishment of new dealership networks, the "highly discriminatory" commodity tax, and high homologation costs – account for most of the disparity. Japan also imposes a discriminatory road tax, which is significantly higher for larger engine vehicles, and maintains a more complicated and time-consuming approval process for imported automobiles. **Because of such barriers, throughout the 1970s, import penetration into the Japanese market averages 1%**.

- **American auto part companies also face great difficulty** because Japanese vehicle manufacturers purchase parts primarily through industrial groupings, or *keiretsu*, that include only Japanese parts producers. Foreign parts companies are excluded from distribution systems and from the crucial design phase of new vehicle development. Japanese support programs and protectionist standards, packaging, and documentation requirements also make breaking into the Japanese market very difficult.

1980s Following bilateral negotiations over the rapid expansion of Japanese exports and the closure of the Japanese market to U.S. autos and parts, Japan announces that it will **limit the export of motor vehicles**. In response, Japanese vehicle manufacturers take advantage of open U.S. investment policies to establish "transplant" facilities in the United States. In 1982, Honda opens a joint venture in Ohio, followed by Nissan, Toyota, Mazda, Mitsubishi, and Subaru-Isuzu. These vehicle manufacturers do not purchase parts from U.S. auto parts suppliers but, instead, import from Japan. Later, the transplant companies bring their *keiretsu* auto parts suppliers into the United States. **U.S. auto parts companies now face the same problems of access in the United States market that they had previously only experienced in Japan**.

1986 President Reagan launches the **Market-Oriented Sector-Specific (MOSS) Talks on Transportation Machinery** to address market access barriers with respect to auto parts. Japanese auto manufacturers commit to collect and submit data regarding their sourcing for tracking purposes and to cooperate with the U.S. government and parts suppliers on sales promotion activities. The Japanese government commits to clarifying that installation of foreign-made parts should "not pose any obstacle" to passing the required periodic inspection for passenger vehicles (*shaken*).

In 1988, GAO reports that "auto parts experts we interviewed did not have great expectations that the MOSS talks would lead to dramatic changes in the general business environment in Japan." **This skepticism is borne out as the auto parts deficit grows after the agreement, from $7.3 billion in 1987 to $10 billion in 1989.**

1989 President Bush launches the **Structural Impediments Initiative (SII)** targeting Japanese barriers, many of which are critical in the auto sector -- *keiretsu* relationships, exclusionary business practices such as the formation of cartels, and business pricing practices under which Japanese companies would sell products at a premium in Japan and price low in the U.S. market. Most recommendations focus on development, and stricter enforcement, of anti-competition laws and policies.

1994 A joint study commissioned by the U.S. and Japan under the MOSS framework finds that "a variety of factors make it extremely difficult for foreign vehicles to compete in the Japanese automotive market" including exclusive dealerships-manufacturer relationships, non-economic consumer behavior, preferential government regulations, high costs of entering the automotive sales market, high costs of certification, and discriminatory access to key market information. **Auto import penetration in Japan, notwithstanding the SII and other initiatives, remains less than 5%.**

1995 President Clinton signs **U.S.-Japan Auto Agreement** to address continuing barriers in the automobile and parts sectors and to promote deregulation of the auto parts aftermarket. With respect to automobiles, there is particular focus, once again, on exclusionary relationships between Japanese automakers and dealers. With respect to auto parts, there is focus, yet again, on exclusionary relationships between auto parts suppliers and Japanese automakers.

1998 The yen begins to weaken immediately following signing of the Auto Agreement, from 94.7 in August 1995 to 144.68 yen/dollar by August 1998. **Japan subsequently begins to intervene massively in the currency markets to maintain a weak yen** (from 1998 to 2004, Japan purchases half a trillion dollars, intervening more than 160 times). This provides a massive subsidy to Japanese automakers and places exports at an enormous disadvantage in the Japanese market.

1999 **The U.S. Commerce Department, in its last report on implementation of the Auto Agreement, writes: "we are disappointed with the overall Japanese Government actions to open and deregulate its automotive market."** Commerce notes the "continued reluctance of some Japanese dealers to carry foreign vehicles for fear of damaging their long-term relationships with Japanese manufacturers" and urges "further proactive actions by the Japanese Government and Japanese automakers . . . to ensure that restrictive business practices in this sector are fully eliminated."

2000s **Total auto import penetration into the Japanese market remains at approximately 5%, the same levels as before the 1995 Auto Agreement**.

2012 **Toyota complains of "six woes"** -- **strong yen**, high corporate taxes, **delay in free trade agreements**, restrictions on the use of temporary workers in manufacturing, environmental regulations, and energy shortages following the Great East Japan Earthquake – and threatens to offshore production if these concerns are not addressed. The Japanese Automobile Manufacturers Association (JAMA) states: "JAMA strongly advocates continued measures aimed at correcting the excessive strength of the yen, as well as decisive steps to advance, on an equal footing, the Trans-Pacific Partnership and other free trade-promoting economic accords." Prime Minister Abe commits to monetary policies designed to weaken the yen.

2013 **Japan formally announces intent to join Trans-Pacific Partnership negotiations** with the United States and begins EU negotiations.